



## **REPORT OF THE AUDITOR-GENERAL TO THE NORTH WEST PROVINCIAL LEGISLATURE AND THE COUNCIL OF THE MORETELE LOCAL MUNICIPALITY**

### **REPORT ON THE FINANCIAL STATEMENTS**

#### **Introduction**

1. I have audited the financial statements of the Moretele Local Municipality set out on pages XX to XX, which comprise the statement of financial position as at 30 June 2014, the statement of financial performance, the statement of changes in net assets, the cash flow statement and the statement of comparison of budget and actual amounts for the year then ended, as well as the notes, comprising a summary of significant accounting policies and other explanatory information.

#### **Accounting officer's responsibility for the financial statements**

2. The accounting officer is responsible for the preparation and fair presentation of these financial statements in accordance with South African Standards of Generally Recognised Accounting Practice (SA Standards of GRAP), the requirements of the Municipal Finance Management Act of South Africa, 2003 (Act No. 56 of 2003) (MFMA) and the Division of Revenue Act of South Africa, 2013 (Act No. 2 of 2013) (DoRA) and for such internal control as the accounting officer determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

#### **Auditor-general's responsibility**

3. My responsibility is to express an opinion on these financial statements based on my audit. I conducted my audit in accordance with the Public Audit Act of South Africa, 2004 (Act No. 25 of 2004) (PAA), the general notice issued in terms thereof and International Standards on Auditing. Those standards require that I comply with ethical requirements, and plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.
4. An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgement, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.
5. I believe that the audit evidence I have obtained is sufficient and appropriate to provide a basis for my qualified audit opinion.

#### **Basis for qualified opinion**

##### **Property, plant and equipment**

6. I was unable to obtain sufficient appropriate audit evidence for property, plant and equipment as not all assets could be physically verified and located to the asset register. In addition, I was unable to adequately determine the valuation for infrastructure assets due to the incorrect

discounting rate used in the valuation of these assets. Consequently I was unable to determine whether any adjustments relating to property plant and equipment of R1 046 171 371 (2013: R1 033 114 487) disclosed in note 8 to the financial statement, was necessary. Additionally, these misstatements also resulted in the misstatement of asset depreciation of R85 206 262 (2013: R82 318 446) and impairment expenses of R525 350 disclosed in notes 22 and 23 to the financial statements, respectively.

#### **VAT receivable**

7. I was unable to obtain sufficient appropriate audit evidence for the VAT receivable for the current and prior years as a result of an inadequate system to reconcile the VAT receivable and the actual VAT amounts claimed. The VAT receivable could not be confirmed by alternative means. Consequently, I was unable to determine whether any adjustment to VAT receivable of R5 616 697 (2013: R7 949 659) disclosed in note 6 to the financial statements, was necessary.

#### **Revenue**

8. The municipality did not bill all water usage due to the lack of appropriate systems in place. I was unable to adequately determine the extent of the misstatement on revenue from service charges of R24 961 627 (2013: R19 180 404) disclosed in note 14 to the financial statements. As a consequence of this misstatement, the receivables of R 59 016 988 disclosed in note 7 to the financial statements, is also misstated.

#### **Receivables from exchange transactions**

9. The municipality did not adequately assess consumer debtors, individually or by category, for any indication that these assets may be impaired in accordance with SA Standards of GRAP, GRAP 104, *Financial instruments*. I was unable to practicably determined the resulting misstatement on receivables from exchange transaction of R59 016 988 (2013: R95 288 241), the related provision for doubtful debts of R40 938 173 (2013: R26 281 858) disclosed in note 7 to the financial statements, nor the resultant impact on the accumulated surplus.

#### **Cash flow statement**

10. I was unable to obtain sufficient appropriate audit evidence for cash flows from investing activities of R100 237 466 (2013: R96 587 971) due to the inclusion of prior year work in progress as cash flows in the current year and could not be confirmed by alternative means. Consequently, I was unable to determine whether any adjustments to the cash flow statement was necessary.

#### **Irregular expenditure**

11. Section 125 of the MFMA requires that the financial statements include particulars of all irregular expenditure incurred during the current and the prior financial years. During the audit it was found that the municipality made payments of R653 824 in contravention of the supply chain management regulations which were not included in irregular expenditure disclosed in note 39 to the financial statements. As the municipality did not quantify the full extent of the irregular expenditure, it was impracticable to determine the resultant understatement of irregular expenditure of R378 879 997 disclosed in note 39 to the financial statements.

#### **Material losses**

12. I was unable to obtain sufficient appropriate audit evidence for water distribution losses of R27 188 613 (2013: R32 653 649) disclosed in note 25 to the financial statements as required by section 125(2)(d)(i) of the MFMA. The extent of the distribution losses could not be confirmed by alternative means. Consequently, it was unable to determine whether any adjustment to this disclosure of material losses was necessary.



### **MFMA disclosure**

13. The municipality did not include particulars of non-compliance with the MFMA in the accounting officer's report and/or the notes to the financial statements, as required by section 125(2)(e) of the MFMA.

### **Qualified opinion**

14. In my opinion, except for the effects of the matters described in the basis for qualified opinion paragraphs, the financial statements present fairly, in all material respects, the financial position of the Moretele Local Municipality as at 30 June 2014 and its financial performance and cash flows for the year then ended, in accordance with SA Standards of GRAP and the requirements of the MFMA and the DoRA.

### **Emphasis of matters**

15. I draw attention to the matters below. My opinion is not modified in respect of these matters.

### **Unauthorised, fruitless and wasteful expenditure**

16. As disclosed in note 37 to the financial statements, unauthorised expenditure of R61 652 970 was incurred in the current year and the unauthorised expenditure of R56 296 610 from prior years had not yet been dealt with in accordance with section 32 of the MFMA.
17. As disclosed in note 38 to the financial statements, fruitless and wasteful expenditure of R118 910 was incurred in the current year and fruitless and wasteful of R11 216 173 from prior years not yet been dealt with in accordance with section 32 of the MFMA.

### **Restatement of corresponding figures**

18. As disclosed in note 34 to the financial statements, the corresponding figures for 2013 have been restated as a result of an error discovered during 2014 in the financial statements of the Moretele Local Municipality at, and for the year ended 30 June 2013.

### **Significant uncertainties**

19. With reference to note 32 to the financial statements, the municipality is the defendant in a number of legal claims. The municipality is opposing these claims based on legal advice from the municipality's legal counsel. The ultimate outcome of these matters cannot presently be determined and no provision for any liability that may result has been made in the financial statements.

### **Additional matter**

20. I draw attention to the matter below. My opinion is not modified in respect of this matter.

### **Unaudited supplementary schedules**

21. The supplementary information set out on pages XX to XX does not form part of the financial statements and is presented as additional information. I have not audited these schedules and accordingly I do not express an opinion thereon.

## **REPORT ON OTHER LEGAL AND REGULARITY REQUIREMENTS**

22. In accordance with the PAA and the general notice issued in terms thereof, I report the following findings on the reported performance information against predetermined objectives for the selected strategic objectives presented in the annual performance report, non-compliance with legislation as well as internal control. The objective of my tests was to identify reportable findings as described under each subheading but not to gather evidence to express assurance on these matters. Accordingly, I do not express an opinion or conclusion on these matters.

## **Predetermined objectives**

23. I performed procedures to obtain evidence about the usefulness and reliability of the reported performance information for the following selected strategic objectives presented in the annual performance report of the municipality for the year ended 30 June 2014:
- To ensure water provision to all households on pages XX to XX
  - To provide access to portable sanitation to all communities on pages XX to XX
  - To provide accessible roads to all communities on pages XX to XX
  - Eskom household electrification on pages XX to XX
  - To provide low cost housing to all communities on pages XX to XX
  - To develop and regulate cemeteries on pages XX to XX
  - To increase the number of libraries within Moretele Local Municipality on pages XX to XX
24. I evaluated the reported performance information against the overall criteria of usefulness and reliability.
25. I evaluated the usefulness of the reported performance information to determine whether it was presented in accordance with the National Treasury's annual reporting principles and whether the reported performance was consistent with the planned strategic objectives. I further performed tests to determine whether indicators and targets were well defined, verifiable, specific, measurable, time bound and relevant, as required by the National Treasury's Framework for managing programme performance information (FMPPI).
26. I assessed the reliability of the reported performance information to determine whether it was valid, accurate and complete.
27. The material findings in respect of the selected strategic objectives are as follows:

### **To ensure water provision to all households**

#### **Usefulness of reported performance information**

28. The FMPPI requires that indicators be well defined and verifiable and targets be specific, measureable and time bound:
- A total of 66% of the targets were not specific.
  - The required performance for 67% of the targets could not be measured.
  - Significantly important indicators were not well defined.
  - A total of 100% of the indicators were not verifiable.
29. This was because management was not trained in the requirements of the FMPPI and due to a lack of proper technical indicator descriptions and effective monitoring systems and processes

#### **Reliability of reported performance information**

30. The FMPPI requires auditees to have appropriate systems to collect, collate, verify and store performance information to ensure valid, accurate and complete reporting of actual achievements against planned objectives, indicators and targets. The reported performance information was not valid, accurate and complete when compared to the source evidence provided. This was due to a lack of standard operating procedures and technical indicator descriptions for the accurate measurement, recording and monitoring of performance frequent review of the validity of reported achievements against source documentation.

### **To provide access to portable sanitation to all communities**

#### **Usefulness of reported performance information**

31. The FMPPI requires that indicators be well defined and verifiable and targets be specific, measureable and time bound:
- A total of 29% of the targets were not specific.





- The required performance for 29% of the targets could not be measured.
  - Significantly important indicators were not well defined.
  - A total of 100% of the indicators were not verifiable.
32. This was because management was not trained in the requirements of the FMPPI and due to a lack of proper technical indicator descriptions and effective monitoring systems and processes

#### **Reliability of reported performance information**

33. The FMPPI requires auditees to have appropriate systems to collect, collate, verify and store performance information to ensure valid, accurate and complete reporting of actual achievements against planned objectives, indicators and targets. The reported performance information was not valid, accurate and complete when compared to the source evidence provided. This was due to a lack of standard operating procedures and technical indicator descriptions for the accurate measurement, recording and monitoring of performance frequent review of the validity of reported achievements against source documentation.

#### **To provide accessible roads to all communities**

##### **Usefulness of reported performance information**

34. The FMPPI requires that indicators be well defined and verifiable and targets be specific, measureable and time bound:
- Significantly important indicators were not well defined.
35. This was because management was not trained in the requirements of the FMPPI and due to a lack of proper technical indicator descriptions and effective monitoring systems and processes

##### **Reliability of reported performance information**

36. The FMPPI requires auditees to have appropriate systems to collect, collate, verify and store performance information to ensure valid, accurate and complete reporting of actual achievements against planned objectives, indicators and targets. The reported performance information was not valid, accurate and complete when compared to the source evidence provided. This was due to a lack of standard operating procedures and technical indicator descriptions for the accurate measurement, recording and monitoring of performance frequent review of the validity of reported achievements against source documentation.

#### **Eskom household electrification**

##### **Usefulness of reported performance information**

37. Section 41(c) of the Municipal Systems Act, 2000 (Act No. 32 of 2000) (MSA) requires the integrated development plan (IDP) to form the basis for the annual report, therefore requiring consistency of objectives, indicators and targets between planning and reporting documents. All the reported strategic objectives were not consistent with those in the approved IDP. This was due to the lack of review for consistency of the information reported against the integrated development plan.
38. The FMPPI requires that indicators be well defined and verifiable and targets be specific, measureable and time bound:
- A total of 50% of the targets were not specific.
  - The required performance for 50% of the targets could not be measured.
  - Significantly important indicators were not well defined.
  - All total of 100% indicators were not verifiable.

39. This was because management was not trained in the requirements of the FMPPI and due to a lack of proper technical indicator descriptions and effective monitoring systems and processes.

#### **Reliability of reported performance information**

40. The FMPPI requires auditees to have appropriate systems to collect, collate, verify and store performance information to ensure valid, accurate and complete reporting of actual achievements against planned objectives, indicators and targets. I was unable to obtain the information and explanation I consider necessary to satisfy myself as to the reliability of the reported performance information. This was due to the inclusion of the performance indicators which are not under the direct control of the municipality.

#### **To provide low cost housing to all communities**

##### **Usefulness of reported performance information**

41. The FMPPI requires performance indicator to relate logically and directly to an aspect of the auditees mandate and the realisation of strategic goals and objectives. 100% of the indicators did not fall within the control of the municipality. The relevance of the performance indicators could not be assessed due to the performance indicator not under the direct control of the municipality.

##### **Reliability of reported performance information**

42. The FMPPI requires auditees to have appropriate systems to collect, collate, verify and store performance information to ensure valid, accurate and complete reporting of actual achievements against planned objectives, indicators and targets. I was unable to obtain the information and explanations I considered necessary to satisfy myself as to the reliability of the reported performance information. This was due to the inclusion of the performance indicators which are not under the direct control of the municipality.

#### **To develop and regulate cemeteries**

##### **Usefulness of reported performance information**

43. The FMPPI requires performance indicator to relate logically and directly to an aspect of the auditees mandate and the realisation of strategic goals and objectives. 100% of the indicators did not fall with the control of the municipality. The relevance of the performance indicators could not be assessed due to the performance indicator not under the direct control of the municipality

##### **Reliability of reported performance information**

44. The FMPPI requires auditees to have appropriate systems to collect, collate, verify and store performance information to ensure valid, accurate and complete reporting of actual achievements against planned objectives, indicators and targets. I was unable to obtain the information and explanations I considered necessary to satisfy myself as to the reliability of the reported performance information. This was due to the inclusion of the performance indicators which are not under the direct control of the municipality.

#### **To increase the number of libraries within Moretele Local Municipality**

##### **Usefulness of reported performance information**

45. The FMPPI requires performance indicator to relate logically and directly to an aspect of the auditees mandate and the realisation of strategic goals and objectives. 100% of the indicators did not fall with the control of the municipality. The relevance of the performance indicators could not be assessed due to the performance indicator not under the direct control of the municipality



## **Reliability of reported performance information**

46. The FMPPI requires auditees to have appropriate systems to collect, collate, verify and store performance information to ensure valid, accurate and complete reporting of actual achievements against planned objectives, indicators and targets. I was unable to obtain the information and explanations I considered necessary to satisfy myself as to the reliability of the reported performance information. This was due to the inclusion of the performance indicators which are not under the direct control of the municipality.

## **Additional matter**

47. I draw attention to the following matter:

## **Achievement of planned targets**

48. Refer to the annual performance report on pages XX to XX for information on the achievement of the planned targets for the year. This information should be considered in the context of the material findings on the usefulness and reliability of the reported performance information for the selected strategic objectives reported in paragraphs 28 to 46 of this report.

## **Compliance with legislation**

49. I performed procedures to obtain evidence that the municipality had complied with applicable legislation regarding financial matters, financial management and other related matters. My findings on material non-compliance with specific matters in key legislation, as set out in the general notice issued in terms of the PAA, are as follows:

## **Strategic planning and performance management**

50. The performance management system and related controls were inadequate as it did not describe and represent the processes of performance planning, monitoring, measurement, review, reporting and improvement and how it is conducted, organised and managed, including determining the roles of the different role-players, as required by section 38 of the MSA and regulation 7 of the Municipal planning and performance management regulations.
51. The local community was not afforded the opportunity to comment on the final draft of the integrated development plan before adoption, as required by section 42 of the MSA and regulations 9, 13(1), 13(4) (c) and 15(3) of the Municipal planning and performance management regulations.
52. Measurable performance targets for the financial year with regard to each of the strategic objectives and key performance indicators were not set in the IDP, as required by section 41(1)(b) of the MSA and the Municipal planning and performance management regulations 12(1) and 12(2)(e).

## **Annual financial statements**

53. The financial statements submitted for auditing were not prepared in all material respects in accordance with the requirements of section 122 of the MFMA. Material misstatements of liabilities, expenditure and disclosure items identified by the auditors in the submitted financial statements were subsequently corrected and the supporting records were provided, but the uncorrected material misstatements resulted in the financial statements receiving a qualified audit opinion.

## **Expenditure management**

54. Reasonable steps were not taken to prevent unauthorised expenditure; irregular expenditure; fruitless and wasteful expenditure, as required by section 62(1) (d) of the MFMA.

## **Procurement and contract management**

55. The municipality did not implement a SCM policy as required by section 111 of the MFMA.

56. Goods and services with a transaction value of below R200 000 were procured without obtaining the required price quotations as required by SCM regulations 17(a) and (c).
57. Sufficient appropriate audit evidence could not be obtained that contracts and quotations were awarded to bidders based on points given for criteria that were stipulated in the original invitation for bidding and quotations, as required by SCM Regulations 21(b) and 28(1)(a) and Preferential Procurement Regulations.
58. Sufficient appropriate audit evidence could not be obtained that contract and quotations were only awarded to providers whose tax matters have been declared by the South African Revenue Service to be in order as required by SCM regulation 43.
59. The prospective providers list for procuring goods and services through quotations was not updated at least quarterly to include new suppliers that qualify for listing, and prospective providers were not invited to apply for such listing at least once a year as per the requirements of SCM regulation 14(1)(a)(ii) and 14(2).
60. Awards were made to providers who are in the service of other state institutions or whose directors/ principal shareholders are in the service of other state institutions, in contravention of MFMA 112(j) and SCM regulations 44. Similar awards were identified in the prior year and no effective steps were taken to prevent or combat the abuse of the SCM process in accordance with SCM regulation 38(1).
61. Sufficient appropriate audit evidence could not be obtained that contracts and quotations were awarded only to bidders who submitted a declaration on whether they are employed by the state or connected to any person employed by the state, as required by SCM regulation 13(c).

#### **Consequence management**

62. Unauthorised, irregular, fruitless and wasteful expenditure incurred by the municipality was not investigated to determine the person liable for the expenditure, in accordance with the requirements of section 32(2) of the MFMA.

#### **Revenue management**

63. A credit control and debt collection policy was not implemented, as required by section 96(b) of the MSA and section 62(1)(f)(iii) of MFMA.
64. An adequate management, accounting and information system which accounts for revenue and debtors was not in place, as required by section 64(2)(e) of the MFMA.
65. An effective system of internal control for revenue was not in place, as required by section 64(2)(f) of the Municipal Finance Management Act.

#### **Liability management**

66. An effective system of internal control for liabilities was not in place, as required by section 63(2) (c) of the MFMA.

#### **Asset management**

67. An effective system of internal control for assets (including an asset register) was not in place, as required by section 63(2) (c) of the MFMA
68. Capital assets were permanently disposed of without the approval of the council and, as required by section 14(2)(a) of the MFMA.

#### **Budget**

69. Expenditure was incurred in excess of the limits of the amounts provided for in the votes of the approved budget, in contravention of section 15 of the MFMA.

#### **Internal audit**

70. The internal audit unit did not function as required by section 165(2) of the MFMA, in that:





- it did not report to the audit committee on the implementation of the internal audit plan.
- it did not advise the accounting officer and report to the audit committee on matters relating to internal controls; accounting procedures and practices; risk and risk management.

71. The internal audit unit did not advise the accounting officer and report to the audit committee on matters relating to compliance with the MFMA, the DoRA and other applicable legislation, as required by section 165(2)(b)(vii) of the MFMA.

#### **Audit committee**

72. The audit committee did not advise the council and accounting officer on matters relating to internal financial control and risk management and performance evaluation as required by section 166(2)(a) of the MFMA.

73. The audit committee did not advise the council and accounting officer on matters relating to the adequacy, reliability and accuracy of financial reporting and information, as required by section 166(2)(a)(iv) of the MFMA.

74. The audit committee did not advise the council and accounting officer on matters relating to compliance with legislation, as required by section 166(2)(a)(vii) of the MFMA.

75. The audit committee did not respond to the council on the issues raised in the audit reports of the Auditor-General, as required by section 166(2)(c) of the MFMA.

#### **Waste management**

76. The municipality operated its 4 waste disposal sites and wastewater treatment facility without a license in contravention of section 20(b) of the National Environmental Management Waste Act, 2008 (Act No. 59 of 2008) (NEMWA), section 24(2)(a) of the National Environmental Management Act, 1998 (Act No. 107 of 1998) (NEMA) and section 22(1)(b) of the National Water Act, 1998 (Act No. 36 of 1998) (NWA).

77. The municipality's operational activities at its waste disposal sites and wastewater treatment facility contravened or failed to comply with the requirements of a waste management license, sections 67(1)(f) and (h) of the NEMWA and sections 151(1)(c) and (i) of the NWA.

78. The municipality's waste management and disposal activities contravened or failed to comply with the requirements of section 28(1) of the NEMA, section 19 of the NWA and sections 16(1)(c) and (d) and 26(1)(b) of the NEMWA.

79. The municipality did not exercise its legislative and executive authority as required by sections 11(3)(l) and (m) of the MSA by managing, monitoring and enforcing environmental related bylaws to promote a safe and healthy environment.

#### **Internal control**

80. I considered internal control relevant to my audit of the financial statements, performance report and compliance with legislation. The matters reported below are limited to the significant internal control deficiencies that resulted in the basis for qualified opinion, the findings on the performance report and the findings on non-compliance with legislation included in this report

#### **Leadership**

81. Leadership did not ensure that the performance of the municipality was sufficiently measured against predetermined objectives as required by the MFMA. In addition, the municipality did not comply with all the key legislation resulting in material non-compliance as reported above.

#### **Financial and performance management**

82. Management failed to implement effective controls to ensure that information in the financial statements and the report on predetermined objectives were reliable before submission for audit. Management could not provide evidence in support of the information presented in the

annual performance report and documents were not submitted to verify compliance with legislation.

## Governance

83. The audit committee did not ensure that the risk assessment of the municipality was performed to ensure that risks relating to the municipality were identified and addressed. The audit committee also did not ensure that internal audit fulfil its function resulting in the municipality's internal control environment over performance information and compliance with laws and regulations remaining ineffective.

## OTHER REPORTS

### Investigations

84. There is an ongoing investigation conducted by the special investigation unit in supply chain management irregularities. This investigation was not complete at the date of this report.
85. There is an ongoing investigation conducted by the Hawks in supply chain management irregularities. This investigation was not complete at the date of this report.
86. There is an ongoing investigation conducted by the South African Police Services in supply chain management irregularities. This investigation is not yet complete at the date of this report.

Auditor-General

Rustenburg

30 November 2014



AUDITOR - GENERAL  
SOUTH AFRICA

*Auditing to build public confidence*